IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

EMTEC, INC.	:	CIVIL ACTION
	:	
v.	:	
	:	
CONDOR TECHNOLOGY SOLUTIONS, INC, SCM LLC d/b/a THE COMMONWEALTH GROUP, J. MARSHALL COLEMAN and KENNARD F. HILL	:	NO. 97-6652

MEMORANDUM AND ORDER

HUTTON, J. May 13, 1998

Presently before the Court are the Defendants' Motion to Compel Compliance with Subpoena Duces Tecum (Docket No. 10), non-party Deloitte & Touche LLP's Affidavit in Response (Docket No. 11), the Defendants' Supplemental Submission (Docket No. 14), and the Plaintiff's Memorandum in Opposition to Defendants' Motion to Compel (Docket No. 15). For the reasons that follow, the Defendants' Motion to Compel is granted.

I. BACKGROUND

This action arose when the Defendants excluded Plaintiff Emtec, Inc. from participating in a "roll-up IPO" transaction. In the transaction, the parties employed Defendant Condor Technology Solutions, Inc. ("Condor") to effect a consolidation by making an initial public offering of Condor stock and using the proceeds to finance the simultaneous acquisition of eight information technology companies. Emtec was to be the ninth.

According to the Complaint, the transaction was the

brainchild of Emtec and Defendant SCM LLC d/b/a The Commonwealth Group ("Commonwealth"), both information technology companies pursuing a strategy of growth by acquisition. Each had already made a number of acquisitions, and was planning more, when the two discovered each other and decided to merge. But instead of just merging, Commonwealth and Emtec planned a transaction that would accomplish (1) the merger; (2) the acquisition of eight smaller companies; and (3) an initial public offering of common stock.

In its Complaint, Emtec states that before meeting with Commonwealth, it had already obtained all the necessary approvals to acquire two companies, Computer Hardware Maintenance Company, Inc. ("CHMC") and Corporate Access, Inc. ("Corporate Access"). When Emtec and Commonwealth began negotiating the roll-up IPO, Emtec agreed to disclose the identities of CHMC and Corporate Access and include them among the nine companies to be rolled into the consolidated entity. The parties also agreed in a May 13, 1997 letter agreement between Commonwealth and Emtec's financial advisor, Legg Mason Wood Walker, Inc., that in no event would Commonwealth enter into any transactions with either CHMC or Corporate Access without Emtec's approval before May 13, 1999.[1]

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[1] The May 13, 1997 letter agreement, attached as Exhibit B to the Complaint, states in part:

> Commonwealth and Legg Mason have determined to continue to explore a possible business transaction relating to Legg Mason's client EMTEC, Inc. ("EMTEC") and Commonwealth's client The Condor Group ("Condor").

As the roll-up transaction approached its target date, however, the Defendants excluded Emtec and completed the transaction with the other acquirees--including CHMC and Corporate Access--on February 5, 1998. Emtec claims that this was an outright breach of the May 13 agreement and sues for breach of contract, tortious interference with business relations, and misappropriation of a trade secret. The Defendants argue that they excluded Emtec, among other reasons, because it failed to provide them with audited 1997 financial statements establishing a "clean bill of financial health."

II. DISCUSSION

Presently before the Court is the Defendants' Motion to Compel Emtec's accountant, Deloitte & Touche ("D&T"), to comply with a Subpoena Duces Tecum seeking documents relating to D&T's 1997 audit of Emtec. The Defendants state that they need this information to demonstrate Emtec's poor financial condition at the relevant time, and to establish that Emtec's CEO, Thomas

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> Each of EMTEC and Condor have been having discussions with potential acquisition candidates ("Founding Companies") which are engaged in their respective lines of business. Commonwealth and Legg Mason and representatives of EMTEC and Condor propose to meet to discuss a potential business transaction which would require disclosure of information relating to EMTEC's and Condor's Founding Companies.
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> Commonwealth and Legg Mason each hereby agrees that neither it nor Condor or EMTEC, as the case may be, will seek, directly or indirectly, to enter into a business transaction with any of the other's Founding Companies for a period of two years from the date hereof, without the prior written consent of the other party.

Dresser, lied about Emtec's poor condition.

In response, D&T and Emtec argue that Emtec's financial condition is irrelevant to the determination of the action because all that matters is whether the Defendants entered the transaction with CHMC and Corporate Access in violation of their agreement not to. That is, even if the Defendants were justified in excluding Emtec, they breached the contract by consolidating with CHMC and Corporate Access anyway.

Under Federal Rule of Civil Procedure 26(b)(1), parties may obtain discovery of "any matter, not privileged, which is relevant to the subject matter involved in the pending action....The information sought need not be admissible at the trial if the information sought appears reasonably calculated to lead to the discovery of admissible evidence." Under this liberal standard, material is relevant if it bears on, or reasonably could bear on, any issue that is or may be involved in the litigation. See Stainless Broadcasting Co. v. Guzewicz, 1997 U.S. Dist. LEXIS 16849, *1 (E.D.Pa. October 21, 1997) (citing Oppenheimer Fund, Inc. v. Sanders, 437 U.S. 340, 350 (1978)). Although there is some merit to Plaintiff's argument, the Court finds that under this standard the Defendants are entitled to explore Emtec's culpability in the matter, at the very least in support their affirmative defenses.

D&T and Emtec claim, however, that Pennsylvania's statutory accountant-client privilege, 63 Pa. Cons. Stat. Ann. § 9.11a (1997), bars such discovery when directed at a party's

accountant.[2] See Rhone-Poulenc Rorer Inc. v. Home Indem. Co., 32 F.3d 851, 861 (1994) (finding state law privileges apply to state law claims under Federal Rules of Evidence 501 and 1101(c)). In response, the Defendants argue that although the privilege applies on its face, it does not protect D&T from the present subpoena for two reasons: (1) Emtec has waived the privilege by producing documents and offering deposition testimony as to the substance of the audit; and (2) the present subpoena falls within the "court of law" exception contained within the exclusionary portion of the statute. Under the circumstances of the case, the Court agrees with the Defendants that Emtec has waived its privilege as to any materials, and any communications it had with D&T, relating to Emtec's 1997 financial statements.

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[2] This statute establishes a general privilege, from which it carves out a specific exclusion. The general accountant-client privilege states:

> Except by permission of the client engaging him or the heirs, successors or personal representatives of a client, a licensee or a person employed by a licensee shall not be required to, and shall not voluntarily, disclose or divulge information of which he may have become possessed unless the sharing of confidential information is within the peer review process....The information derived from or as the result of such professional services shall be deemed confidential and privileged.

Id. The exclusion states:

> Nothing in this section shall be taken or construed as prohibiting the disclosure of information required to be disclosed by the standards of the profession in reporting on the examination of financial statements, or in making disclosures in a court of law or in disciplinary investigations or proceedings when the professional services of the certified public accountant, public accountant, or firm are at issue in the action, investigation or proceeding in which the certified public accountant, public accountant, or firm is a party.

Id.

Pennsylvania's accountant-client privilege belongs to the client, not to the accountant. See Sansom Refining Co. v. Bache Halsey Stuart Shields, Inc., 92 F.R.D. 440, 441 (E.D.Pa. 1981). And as with any other privilege, the client may waive the accountant-client privilege through conduct inconsistent with its assertion.

> When the client commences a lawsuit the allegations of which make relevant information and knowledge in the possession of the accountant and where the information or knowledge would be discoverable from the client if it was in his possession, then the client should be deemed to have waived the privilege by initiating the suit. The privilege could not have been intended to cloak material that would be discoverable from the client if it was in the client's possession. See Greenfield Foundation v. Bankers Securities Corp., 7 Pa.D.&C.3d 535, 543 (C.P. Phila. 1975).

Id. See Stainless Broadcasting, 1997 U.S. Dist. LEXIS 16849, *4; Detroit Coke Corp. v. NKK Chemical USA, Inc., 1993 WL 367060, *2 (W.D.N.Y. September 13, 1993) (discussing waiver of Pennsylvania accountant-client privilege).

In Sansom Refining, 92 F.R.D. at 441, this Court found that a plaintiff implicitly waived its accountant-client privilege by initiating a lawsuit as to which accountant-client communications were material. Deposition testimony established that the accountants had supervised the plaintiff's accounts, and that plaintiff directed them to conduct an internal investigation after discovering the allegedly unauthorized trades. During discovery, the defendant subpoenaed plaintiff's accountants for

information about plaintiff's supervision and trading of its accounts and about the amount of loss plaintiff sustained due to unauthorized trades. Although the plaintiff invoked Pennsylvania's accountant-client privilege, this Court granted the defendant's motion to compel the accountants to comply with the subpoena, finding the plaintiff had waived its privilege by bringing a lawsuit with respect to which its accountants possessed material information. See id.

In Stainless Broadcasting, 1997 U.S. Dist. LEXIS 16849, *4, this Court found that a plaintiff had waived its accountant-client privilege under similar circumstances, where the information sought was "central" to the litigation. In Stainless Broadcasting, the plaintiff corporation brought an action alleging that its former President and CEO had authorized an option agreement harmful to the corporation. In discovery, the defendant subpoenaed the plaintiff's accountants for information concerning the effect of the option on its stock price and the amount of any damages. Citing Sansom, this Court found that the accountants

> were clearly involved in the plaintiff's evaluation and decision-making process regarding the option agreement. Because the option agreement is the central issue in this litigation, and information regarding the option agreement would have been discoverable from plaintiff if it were in its possession, plaintiff is deemed to have waived the accountant-client privilege.

Id. See Detroit Coke, 1993 WL 367060, *2 ("The accountant-client privilege is designed to encourage full divulgence to the

accountant; it should not be used offensively to prevent a sued party's access to relevant and potentially vital information in challenging claims made against the accountant's client.").

In the present case, the Defendants wish to depose D&T, and seek from it "[a]ll documents regarding Emtec, Inc. prepared in connection with the audit and preparation of audited financial statements by Deloit [sic] & Touche of Emtec, Inc. for Emtec, Inc.'s fiscal year ended March 31, 1997, including, but not limited to, any documents referring or relating to a possible 'going concern' qualification." (Def.'s Mot. to Compel at Ex. H). While this information is, itself, perhaps not as central to the elements of the Plaintiff's claims as was the information sought in Sansom and Stainless Broadcasting, it is clearly relevant to a number of the Defendants' Affirmative Defenses. In any case, the Defendants are entitled to this information for the general purpose of developing their defense, and providing the Court and jury with a full account of the events that led to Emtec's exclusion from the transaction.

Finally, the Court cannot agree with D&T that compliance with the subpoena would be unduly burdensome or harassing. The information sought concerns Emtec's 1997 financial statements only. D&T prepared these statements less than a year ago and admits that it has retained its work product. In any case, D&T fails entirely to explain why compliance with the subpoena would be more burdensome in this instance than in any other litigation.

An appropriate Order follows.

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O R D E R

AND NOW, this day of May, 1998, upon consideration of the Defendants' Motion to Compel Compliance with Subpoena Duces Tecum, non-party Deloitte & Touche LLP's Affidavit in Response, the Defendants' Supplemental Submission, and the Plaintiff's Memorandum in Opposition to Defendants' Motion to Compel, IT IS HEREBY ORDERED that the motion is **GRANTED**.

IT IS FURTHER ORDERED that:

(1) Deloitte & Touche shall designate and make available for testimony a witness pursuant to Defendants' Subpoena Duces Tecum, and shall produce for inspection or copying the documents described therein, within twenty (20) days of the date of this Order; and

(2) The discovery period established in the Court's Order of March 3, 1998 is extended as necessary to permit this deposition and document production.

BY THE COURT:

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HERBERT J. HUTTON, J.